Date of Hearing: January 20, 2000

ASSEMBLY COMMITTEE ON JUDICIARY
Sheila James Kuehl, Chair
AB 1221 (Dutra) – As Amended: January 10, 2000

SUBJECT: CONSTRUCTION DEFECTS: HOME WARRANTIES; LITIGATION IMPEDIMENTS

KEY ISSUES:

1) SHOULD THE LEGISLATURE CREATE A HOME CONSTRUCTION WARRANTY PROGRAM WITH THE GOAL OF PROTECTING CONSUMERS FROM CONSTRUCTION DEFECTS IN NEWLY CONSTRUCTED RESIDENTIAL HOMES AND SPURRING CONSTRUCTION OF AFFORDABLE MULTIFAMILY HOUSING?

2) IS THERE SUFFICIENT EVIDENCE LINKING THE DECREASE IN AFFORDABLE MULTIFAMILY HOUSING TO CONSTRUCTION DEFECT LITIGATION?

3) WILL THE CREATION OF HOME CONSTRUCTION WARRANTIES LEAD TO INCREASED AFFORDABLE MULTIFAMILY HOUSING?

4) COULD THIS BILL INADVERTENTLY SLOW THE TIME FOR RESOLUTION OF A CONSTRUCTION DEFECT COMPLAINT RATHER THAN PROVIDE FOR A QUICKER RESOLUTION?

5) SHOULD A SIGNIFICANT HURDLE BE IMPOSED ON HOMEOWNERS BY REQUIRING THEM TO COMPLETE BOTH MANDATORY MEDIATION AND MANDATORY JUDICIAL ARBITRATION BEFORE BEING PERMITTED TO SEEK LEGAL REDRESS IN COURT?

6) DOES THIS BILL PROVIDE CONSUMERS WITH ANY PROTECTIONS AGAINST CONSTRUCTION DEFECTS NOT OTHERWISE GUARANTEED UNDER THE LAW?

7) IF THERE IS A PROBLEM WITH THE CALDERON PROCESS (DESIGNED FOR THE TIMELY RESOLUTION OF CONSTRUCTION DEFECT ACTIONS), WOULD THE BETTER APPROACH BE TO FIX THAT PROCESS INSTEAD OF CREATING AN ENTIRELY SEPARATE PROCESS?

8) DOES THIS BILL INADVERTENTLY EXTEND ITS PROVISIONS TO ALL RESIDENTIAL HOMES AND NOT MERELY CONDOMINIUMS AND TOWNHOUSES, AS INDICATED IN THE BILL'S LEGISLATIVE FINDINGS SECTION?

SUMMARY: Creates the California Homebuyer Protection and Quality Construction Act of 2000 to provide for 10 year home construction warranties for residential properties. Specifically, this bill:

1) Makes the following findings: a) California has a statewide home building crisis; b) despite the tremendous need for multifamily housing (condominiums and townhouses) the construction of this type of housing has all but halted because of construction defect litigation; and c) the great expense of construction defect litigation and the high probability of condominium and townhouse development being subject to construction defect litigation has caused many homebuilders to abandon further development of such housing units.

2) Sets forth its purpose as: promoting the construction of high quality affordable residential housing units; inducing homebuilders to improve the training of new homebuilders to better assure the construction of high quality residential housing; inspiring consumer confidence by establishing standards for residential home warranties that promise high quality workmanship free from construction defects for 10 years; encouraging prompt and fair resolution of construction defect claims by homeowners through the use of consumer friendly claims processing procedures.

3) Authorizes participating homebuilders to offer home construction warranties as a condition of the sale of new residential homes, pursuant to which the homebuilder shall be responsible for the correction of any construction defect covered by the warranty. Such warranties shall last for a minimum of 10 years, with protection under the warranty beginning on the date of substantial completion of the residential home to which it applies. The warranty may not be canceled or changed at any time during the term of the warranty.

4) Provides that, upon proper notice from the homeowner subject to a home construction warranty, the homebuilder shall, for the duration of the period covered by the warranty, be responsible for the correction of any construction defect covered by the warranty. Correction of any construction defect includes repair, replacement, or payment of reasonable costs to repair or replace (based on existing construction codes and standards of construction practice in effect at the time of original construction), or, at the builder's option, rebuilding the structure in accordance with the original plans and specifications or payment of the reasonable value of the property plus relocation costs. The choice as between repair, replacement, or payment is the builder’s.

5) Provides that if a homeowner elects to purchase a home subject to a home construction warranty, "the provisions of that warranty shall be deemed to be the exclusive election of recourse by that homeowner and the participating homebuilder for the claims covered by the warranty. The parties to the warranty contract are deemed to have waived any tort remedies, including negligence, strict liability, implied warranties, or any other common law remedy other than for breach of warranty contract. . . .The homeowner who is party to the warranty contract, should the warranty so provide, waives any noncontractual claims against any design, professional, or trade contractors covered by the warranty who performed professional services or works of improvement on the subject property. This section does not preclude or limit any right of action for bodily injury, wrongful death, or fraud and intentional misrepresentation."

6) Defines construction defect, for purposes of this act, as a defect in design, materials or workmanship that: results from an act or omission of the builder (or a contractor working for the builder); occurs during the original construction of the improvement, or in connection with the

warranty repair work; renders the improvement or some part of it not reasonably fit for its intended purpose; and materially affects building site work, substructure, building shell, or building services.

7) Provides that for a licensed contractor to participate in this homebuyer warranty protection program (and offer such warranties), the contractor must be certified by the Contractor's State License Board (CSLB). In order to be so certified, a builder must: a) hold and maintain a valid license as a general building contractor; b) provide proof of financial security to cover the obligations of the warranty (insurance, a surety bond, or some alternative funding plan); c) demonstrate proof of administrative capacity to administer and process complaints and claims (either in-house, or through contract with an insurance company or warranty administrator); d) develop and implement a quality assurance program meeting specified requirements; e) provide a summary of any alternative dispute resolution process to be used under the warranty.

8) Provides that a contractor shall be deemed to be certified if the CSLB fails to act on a contractor's application within 30 days. The contractor is required to file an annual renewal of the certification, however, the board is required to renew the contractor's certification unless the board finds that the contractor fails to meet any of the above requirements.

9) Provides that any action taken by the CSLB to suspend or revoke the certification of a contractor to issue such warranties shall not affect the obligations of the contractor under any previously issued warranties.

10) Sets forth the following process to seek resolution of construction defect problems for home buyers under a home construction warranty:

    a) The homeowner registers a complaint. The homebuilder or warranty administrator, or licensed insurance company is obligated to acknowledge receipt of an initial nonemergency complaint within 15 days of receipt.

    b) The homebuilder and homeowner schedule a mutually agreeable time for inspection of the condition.

    c) Upon completion of the inspection, and no later than 30 days from receipt of the complaint (unless the parties mutually agree to an extension of time), the homebuilder is required to provide a written statement indicating his or her belief as to whether the condition giving rise to the complaint is covered by the warranty, and any corrective action the builder intends to take to resolve the problem. If the homebuilder determines that the condition is not covered under the warranty, the written statement shall describe the process for filing a claim under the warranty to resolve the dispute.

    d) If a California Home Construction Warranty provides for alternative dispute resolution to resolve disputes under the warranty, the method of dispute resolution shall be mediation with subsequent referral to judicial arbitration. Appointment of a neutral and impartial mediator shall be accomplished within 60 days from the warranty administrator's receipt of a written request

from a homeowner to mediate the claim.

e) If the participants cannot reach an agreement during the mediation, the matter is referred to judicial arbitration. Among the issues to determined by the arbitrator is the reasonableness of offers made or rejected during the mediation – requiring the disclosure of what are otherwise required by law to be confidential mediation proceedings.

f) Either party unsatisfied with the decision of the arbitrator may request a trial de novo, on the facts or the law, after completion of the judicial arbitration.

11) Authorizes any participating homebuilder to offer a warranty, as a condition of the sale of a new residential home, which includes a provision to submit all complaints, claims, disputes, and controversies relating to construction defects, construction deficiencies, or any and all issues arising from the construction of the new residential homes, regardless of the nature of the claim, the injury or damage sustained or the type of remedy sought, to mediation with subsequent referral to judicial arbitration.

12) Permits a home construction warranty to also include a provision to submit any and all disputes or controversies regarding scope of coverage under the warranty or breach of the warranty to mediation with subsequent referral to judicial arbitration, as well as any and all disputes or controversies against a warranty administrator or insurance company.

13) Limits the recovery of a homeowner or homeowner's association that unreasonably rejects an offer made by the builder during the mediation or arbitration process to the reasonable cost of repairs that are necessary to correct the construction defect and are covered under the warranty, and necessary attorney's fees and costs incurred before the offer was rejected. The arbitrator shall determine the reasonableness of the rejection of an offer of a settlement made during the mediation or arbitration.

14) Provides that if a participating builder fails to make a reasonable offer during the mediation or arbitration process, or fails to complete, in a good and workmanlike manner, the repairs specified in an accepted offer, the limitations on damages and remedies provided for under this bill shall not apply. The arbitrator shall determine the reasonableness of an offer of settlement made during the mediation or arbitration.

15) Provides that a home construction warranty transfers to a subsequent purchaser with a transfer of title.

16) Prohibits a participating homebuilder, warranty administrator, or a sales, marketing, or other representative of the homebuilder, from knowingly misrepresenting the terms and conditions of a home construction warranty.

17) Fails, despite the legislative findings of the bill relating specifically to the need for greater multifamily housing (specifically condominiums and townhouses) and the effect of construction defect litigation on this type of housing, to limit the home construction warranties, and concomitant restrictions on

seeking legal redress in the courts, to multifamily housing units.

EXISTING LAW:

1) Provides, as part of the Davis-Stirling Common Interest Development Act, for the establishment and regulation of common interest developments and the homeowner associations which govern such developments. (Civil Code section 1350. All further references are to the Civil Code unless otherwise noted.)

2) Defines common interest development as a condominium project, a community apartment project or other development in which homeowners own a separate interest in their unit and a common interest in the other areas of the development. (Section 1351.)

3) Requires a homeowners' association, prior to commencing an action for damages against a builder of a common interest development based upon a construction or design defect, to give written notice to the builder against whom the claim is made, commencing a mandatory pre-litigation process (known as the "Calderon process"). (Section 1375.)

4) Provides that the pre-litigation process shall not exceed 90 days, unless the parties stipulate to an extension of that time period. During this process, the parties shall try to settle the dispute or attempt to agree to submit it to alternative dispute resolution. (Section 1375.)

5) Requires the board of directors of the association to hold a meeting of association members if the settlement offer is rejected. The meeting must be held at least 15 days prior to the association's commencement of an action for damages against the builder. The notification of the meeting shall be sent to each member at least 15 days before the meeting and shall contain the complete text of the settlement offer, the preliminary list of defects, and the options available to address the problems. (Section 1375.)

6) Imposes a ten (10) year statute of limitations for actions based on latent (hidden) construction defects, and a four (4) year statute of limitations for actions based on patent (obvious) construction defects. (Code of Civil Procedure sections 337.1 and 337.15.)

7) Finds that judicial arbitration is an efficient and equitable method for resolving small claims, and thus requires the court in a county with 10 or more superior court judges, in all civil actions in which the amount in controversy is less than $50,000, to submit the matter to judicial arbitration. In smaller courts, the court may provide by local rule, when it determines that it is in the best interests of justice, that all civil actions in which the amount in controversy is less than $50,000 shall be submitted to judicial arbitration. For civil actions in which the damages exceed $50,000, judicial arbitration may only be provided upon stipulation of the parties. However, any action otherwise subject to judicial arbitration shall be exempt if found by the court not to be amenable to arbitration on the ground that arbitration would not reduce the probable time and expense necessary to resolve the litigation. (Code of Civil Procedure sections 1141.10 and 1141.11, Rule of Court 1600.5.)

8) Provides that an arbitration award shall be final unless a party files a request for a trial de novo within 30 days after the date the arbitrator files the award with the court. A trial de novo may be before a court or a jury, and may be had as to both the law and facts at issue in the arbitration. (Code of Civil Procedure section 1141.20.)

9) Specifies various fees and costs that the party requesting the trial de novo shall be responsible for assuming if the judgment at trial is not more favorable than the arbitration award for the party requesting the trial. (Code of Civil Procedure section 1141.21.)

10) Creates a process whereby courts may order parties in a civil action to mediation, finding that in appropriate cases mediation provides parties with a simplified and economical procedure for obtaining prompt and equitable resolution of their disputes. Such civil action mediation is intended as an alternative judicial arbitration, and neither shall be ordered in cases in which the other is ordered. (Code of Civil Procedure sections 1775 and 1775.4.)

11) Prohibits the court from ordering a case into civil action mediation if the amount in controversy exceeds $50,000. (Code of Civil Procedure section 1775.5.)

12) Provides that determinations of a court to send a case to mediation shall be made by the court after consideration of the expressed views of the parties on the amenability of the case to mediation. Amenability of a particular action for mediation shall be determined on a case-by-case basis, rather than categorically. (Rule of Court 1631.)

13) Provides that no evidence of anything said or any admission made for the purpose of, in the course of, or pursuant to, a mediation is admissible or subject to discovery, and disclosure of the evidence shall not be compelled in any arbitration, administrative adjudication, civil action, or other noncriminal proceeding. All communications, negotiations, or settlement discussions by and between participants in the course of a mediation shall be confidential. (Evidence Code section 1119.)

FISCAL EFFECT: Unknown

COMMENTS: This legislation, previously heard by the Assembly Housing and Community Development Committee, seeks to make substantial changes to the law surrounding construction defects in an attempt to spur new construction of affordable housing. In setting forth the need for this legislation, the author and sponsor provided the Committee with the following statement:

> Although the level of new home construction in California has increased since the downturn of the early and mid 90s, the pent-up demand for new affordable multi-family units is not being met. Some potential home buyers find it difficult to find wanted housing and some who succeed have difficulty getting timely repairs. These problems are caused, in part, by the scarce availability and high cost of insurance that would protect builders from construction defect claims. The California Homebuyer Protection and Quality Construction Act . . . responds to this problem. It is designed to:

- Promote quality construction by subcontractors and tradespeople that meet established standards for experience and training.
- Encourage homebuilders to offer a variety of new home warranties.
- Provide efficient and fair resolution of construction defect disputes.
- Make the development of stacked condominiums and attached townhouses economically feasible once again.

California Research Bureau Finds No Clear Link Between Litigation, Increased Insurance Costs, and Supply of Affordable Housing. At the request of the Assembly Housing & Community Development and Judiciary Committees, and in preparation for the December 1999 interim hearing on this legislation, the California Research Bureau did a preliminary study on the issue of construction defect litigation and its effect on access to affordable multifamily housing. (See California Research Bureau, Construction Defect Litigation and the Condominium Market, November 1999. Hereafter CRB Report.) The CRB Report suggests a definitive lack of evidence to suggest the causal link between construction defect litigation and decrease in access to affordable multifamily housing. The CRB Report notes that although there is "little dispute that the [condominium] market has declined . . . [t]he exact extent and causes of the decline are hard to measure." (Emphasis added.) The CRB Report notes that "real estate professionals state that construction of condominiums largely tracks the overall real estate market." A study of the market over time shows "a pronounced boom during the 1980s, fueled in part by favorable tax treatment that was enacted in 1981. The boom ended in part because of a reversal of the favorable tax laws and overbuilding in many markets. The strong real estate market led to an increase in the price of homes."

The CRB further notes that "[w]hile it is clear that the condominium market has stagnated, it is not clear what is the cause." The CRB offers the following among the possible causes: construction defect litigation; the overall conditions in the real estate market brought about by overbuilding in the 1980s followed by a severe and prolonged recession in California; opposition to new projects by existing neighborhood residents; reluctance on the part of lenders, and their regulators, to finance condominiums because of earlier loan losses; increased affordability of singe-family homes in the 1990s due to falling prices; and preference of home buyers for single-family detached homes. In fact, the CRB Report notes that "as the market is resurging and homes become less affordable, demand for condos is starting to improve. . . .The beginnings of a resurgence in the condo market would tend to bolster the arguments that construction defect litigation has not seriously harmed the market." (Emphasis added.)

With regard to the proponents' assertions that the occurrence of construction defect litigation has exploded in California, and California's construction defect laws are to blame, the CRB Report notes that "[c]ompared to other states, California's statute of limitations are among the longer ones. However, the state's law is by no means extreme or alone in its requirements. . . .There are not readily available statistics on the number of [construction defect] cases. While there are widespread, but difficult to substantiate, claims that litigation has increased, there are unusual factors which may explain the jumps. The years of drought followed by wet winters may have led to an onslaught of claims. The earthquakes in both southern and northern California and the resulting damage and concern over seismic safety may have also led to increased claims. Another factor that may explain any increase in litigation is building on marginal lands. . . Construction is occurring on land that may have greater incidence of environmental problems such as subsidence." (Emphasis added.)

With regard to the availability of insurance, the CRB Report notes that there appears to have been a significant increase in insurance premiums within the state. However, the report concludes, "[t]he apparent significant increase in rates does not necessarily mean that unwarranted litigation is driving the insurance market." (Emphasis added.) The CRB Report concurs with the author's assertion that many insurers have withdrawn from the California market, and exposure to construction defect litigation may very well be a cause. However, although "[c]onstruction defect insurance does appear to be more expensive in California and the policies often are significantly less generous than in other states . . . [i]t is not clear that construction defect litigation is the cause. Housing in California is more expensive, which would lead to somewhat higher rates. Generally, many types of insurance in California are more expensive than in other states. The higher rates may reflect larger losses related to other factors, such as builders not engaging in satisfactory quality control."

Industry-Sponsored Studies on the Relationship Between Construction Defect Litigation and Access to Affordable Housing. The author and proponents of this measure point to two 1996 studies which they believes demonstrate the causal relationship between construction defect litigation and the decrease in access to affordable multifamily housing. In a study of condominium projects in San Diego County, performed at the request of the Building Industry Association of San Diego County, ConAm Economic Research found a correlation between the value of condominiums units and construction defect litigation. The ConAm Report noted that, for similar sized units the resale value for units in litigated projects declined anywhere from 8% to 17%, while the value of units in condominium projects not litigated increased. The ConAm Report also found that a large majority of condominium projects in San Diego County were the subject of litigation – of the 48 projects analyzed, 39, or 81%, had been the subject of litigation.

The comparisons drawn between litigated and non-litigated units, however, do not account for other factors that may have impacted the resale value and saleability of litigated units. For example, the conclusions reached about litigated projects were based on two (2) litigated condominium project in San Diego County. Eight (8) projects comprised the analysis on non-litigated projects. The two litigated projects were substantially larger than the others – with 919 units in the two litigated projects, and 1,391 units in the eight non-litigated projects. The size difference alone could account for differences. Furthermore, the report does not describe the location of the litigated versus the non-litigated projects. Resale values of single family detached houses in the neighborhoods of the two litigated projects may have faced a similar decline.

In its conclusion, the ConAm Report concedes that the small number of projects evaluated makes it findings less than 100% certain. "Although the study is statistically reliable and valid, we would have been more confident in our findings if we could have found a larger sample of both non-litigated projects and projects which had gone through litigation and used their settlement funds to promptly complete reconstruction of project areas enumerated in the litigation action."

Proponents of this bill also point to the industry-sponsored study by the Lusk Center Research Institute at the University of Southern California as evidence of the correlation between construction defect litigation and access to affordable multifamily housing. (Construction Defect Litigation and the Impact on Affordable Housing, July 1996. Hereafter, Lusk Study.) The Lusk Study focused on attached units

(condominiums and townhouses) in nine (9) California counties. Based on interviews with California builders and developers, the Lusk Study found that "[l]awsuits, the threat of lawsuit, and the rise of 'junk' lawsuits all increase defendants' cost of doing business. . . .Our interviews with California developers indicate that they react in three primary ways: they spend money on litigation protection such as independent inspections and videotaping of work-in-progress; they convert attached units and especially stacked flats into lower density single-family detached homes; and they abandon projects in the pipeline prior to construction if they cannot be reconfigured to reduce litigation risk. . . .Our survey of California condominium developers suggest that (other things equal) the prices of new residential condominiums . . . in southern California escalated by $56,500 on average because of litigation expenses and threats." (Emphasis added.)

In its survey of developers, the Lusk Study notes that construction defect litigation is impacting the affordability of housing. The study finds that:

- Seventy-nine percent (79%) of the respondents have faced construction defect litigation.
- Ninety-six percent (96%) of respondents had changed either the price, the size, the number, or the type of units developed because of factors relating to construction defect litigation.
- Sixty-eight percent (68%) of the respondents no longer build townhouses because of factors relating to construction defect litigation.
- Eighty-six percent (86%) of the respondents no longer build stacked units because of factors relating to construction defect litigation.

In reaching these results, the Lusk Center identified and contacted 64 attached-unit developers. Of those, less than one-half (29 developers) responded to the survey. Whether the decision to participate in the survey was guided by a developer's personal experience with construction defect litigation is unknown.

The Lusk Study also notes a decrease in attached unit project starts. "The ratio of attached unit projects started to total projects started has fallen . . . dramatically – from 40% in 1992 to 20% in 1994 and has remained below that level since then. In 1996, only 16% of the new projects included attached units."

With regard to filing of construction defect actions, the Lusk Study acknowledges that "[s]ome of the claims regarding defective products may be legitimate because there was a time in the late eighties when the industry was experiencing a rapid increase in production and many developers were concerned with capturing volume. Some of them sacrificed attention to detail and 'cut corners.'" However, the Lusk Study notes that some of the lawsuits filed and defects alleged were not due to construction of a defective product by a builder, "but rather because the Home Owners Association was negligent in maintaining the property." The Lusk Study concludes that "[a]s a result of these lawsuits, many within the industry have decided to stop building attached/stacked products."

It is important to note that, in commenting on its results, the Lusk Study acknowledged that "[m]any significant factors are impacting the real estate industry, and it is difficult to isolate the effects of construction defect litigation on housing affordability." (Emphasis added.)

Broad Application to All Residential Housing. The primary asserted rationale for the creation of home construction warranties and the concomitant restriction on the ability of homeowners to bring a construction defect action in court is that "despite the tremendous need for condominiums and townhouses, the construction of this type of housing has all but halted because of construction defect litigation." The bill is premised on the need for quality affordable housing, and asserts that this means multifamily housing, specifically condominiums and townhouses. However, the bill has a much greater reach, applying to all residential homes, multifamily and single family, attached and detached units. Unfortunately, the author has not provided the Committee with any evidence suggesting that decreases in the single family housing market that may exist are caused by construction defect litigation and thus that such a dramatic reduction in the rights of home owners to seek redress in court is warranted.

In fact, reports the author points to in support of the assertion that construction defect litigation is a cause in the decline of access to affordable housing, suggest that builders may be turning away from constructing multifamily attached units, such as condominiums and townhouses, and instead building detached multifamily housing, or single family housing. Construction defect litigation, thus is not causing builders to shy away from such projects. These facts suggest there has been no showing that application of the warranty process to such types of residential housing, and restrictions on the ability of homeowners to bring legal action for defects in such buildings, is either necessary or appropriate.

Effect of the Warranty Process on the Timeliness of the Resolution of Construction Defect Disputes. One of the stated primary goals of this legislation is to provide the homeowner with an expedited method to resolve construction defect disputes. However, it is uncertain whether the warranty process created by this bill will in fact have the desired effect. One of the primary criticisms of the current Calderon process (intended to provide for a quicker resolution of construction defect disputes) is that the process takes too long. At the time this Committee considered and approved reforms to the Calderon process (pursuant to AB 1950 (Torlakson, 1998), the Committee heard testimony that contrary to its intended purpose of expeditiously handling construction defect actions, the Calderon process has led to lengthy pre-litigation processes. Parties routinely stipulate to multiple extensions of the 90-day period for fear of appearing unwilling to cooperate in the alternative dispute resolution procedures. One of the proposals to improve the Calderon process was therefore to prohibit multiple extensions of the pre-litigation time period.

Unfortunately, the home construction warranty program created pursuant to this legislation may suffer from the same deficiencies as the Calderon process. The bill allows the parties to "mutually agree" to an extension of time for the builder to respond whether a complaint of a defect alleged by a homeowner is covered under the home warranty. There is no maximum time period contained in the bill for the required mediation of the dispute. The bill only provides that the mediator shall be appointed within 60 days from the warranty administrator's receipt of a written request for mediation. Continuances are similarly allowed in cases referred to judicial arbitration. And since both parties, the builder and the homeowner, are entitled to request a trial de novo after the arbitration award is handed down, the builder has the ability to prolong the process in order to seek a resolution more favorable to him or her.

Another concern with the Calderon process was its failure to include all necessary stakeholders – including subcontractors, materials suppliers, design professionals and insurers – early in the process. This measure would seem to suffer from the same deficiency. Without participation of these players, arguably a homeowner's attempts to fix a defect may be stymied because the party the builder deems responsible for the flaw is not present during the process.

Failure to Work within the Existing Framework. As noted above, there exists in current law a special pre-litigation process, unique to construction defect law, which seeks to encourage expeditious resolution of construction defect claims in common interest developments prior to the filing of a lawsuit. This process, the Calderon process, was enacted into law in 1995. In 1997 and 1998, hearing from all constituency groups that certain problems exist with the Calderon process, Assemblymember Torlakson introduced legislation to improve the process – to provide a system for the timely resolution of disputes, as the process was originally envisioned. One year the legislation was vetoed, and the next year it was stripped down to provisions essentially unrelated to the Calderon process.

The question must still be raised, however, whether it would make greater sense to improve the existing process rather than create an intricate parallel process for resolving construction defect disputes. What this measure does is allow a builder (not a homeowner) to pick and choose – whether to require a homeowner to purchase a home warranty and be restricted to the complaint resolution procedures under the warranty, or to allow the Calderon process to control the resolution of construction defect disputes. The Committee may believe that developing two alternative approaches is unnecessary, and that a better course of action would be to seek to improve the identified problems with the Calderon process.

ARGUMENTS IN SUPPORT: The California Building Industry Association (CBIA), representing over 5,000 firms engaged in light commercial and industrial construction, writes the following in support of this measure:

> AB 1221 would create a voluntary program willing to meet certain requirements for establishing quality control, customer service and a balanced, fair approach to resolving disputes between homeowners and builders. . . .AB 1221 also provides new homeowners and consumers with a mechanism for the timely repair of construction defects when they do arise and decreases costly construction defects litigation.

CBIA further notes that "California should promote more efficient ways to resolve residential construction disputes – the current reliance on litigation has lead to a virtual end to affordably-price attached condominiums and townhouses." CBIA argues that over the last ten years, condominium development has virtually ceased, making affordable homeownership scarce. In order to address these problems, CBIA states that:

> [T]his bill presents an alternative framework for resolving construction disputes by using a voluntary state-sanctioned warranty program AB 1221 establishes minimum warranty standards which require the builder and the warranty administrator to promptly respond to consumer complaints. The legislation offers a higher degree of consumer protection

> by providing more information to the homebuyer about the builders quality control program and customer service program. Moreover, AB 1221 establishes an expedited complaint and claims handling process, as well as a balanced dispute resolution that will provide consumers with what they seek -- an efficient and fair resolution of their claims.

The Civil Justice Association of California (formerly Association for California Tort Reform) also supports the bill, writing: "The state's recent housing boom and increase in property values have illuminated the severe shortage of the most affordable forms of housing: condos and townhouses. Unfortunately, construction defect litigation has made these type of developments unreasonably risky for homebuilders and homebuyers alike. . . .Homeowners and homebuyers deserve a fair, simple and affordable process to make sure needed repairs are made without resorting to costly, lengthy and wasteful litigation. The current dispute resolution process to address construction defects does not offer significant benefits to homeowners involved in such litigation."

Others make the following statements in support of this measure:

This bill would . . . protect both consumers and builders from costly construction defect litigation and encourage the development of quality affordable housing, which there is a severe shortage of.

Costly construction defect litigation adversely impacts the future of quality, affordable housing in California. Reducing the need for litigation by providing equitable ways to repair construction defects will save money and time for everyone involved.

This Act encourages the homebuilding industry to maintain a quality assurance program, improve upon inspection of workmanship and provide for training and continued education of employees.

ARGUMENTS IN OPPOSITION: The California Dispute Resolution Council (CDRC), though taking no position on the general subject of the bill, writes in strong opposition to the section of the bill providing for mediation followed by judicial arbitration, stating that "the most important point of opposition relates to the provisions requiring a subsequent decision maker in a dispute between parties to review offers and information that occurred during a mediation. This would create an enormous exception to mediation confidentiality under current California law as defined in [the] Evidence Code. . . ." CDRC raises additional technical concerns with the mediation and arbitration provisions in the bill, leading to its ultimate suggestion "that the arbitration step be struck from the bill."

The Consumer Attorneys of California, writing in opposition to this measure, note that:

> AB 1221's real effect would be to deny homeowners the ability to recover damages for shoddy construction. . . .Rather than supplementing existing law, the warranty scheme in this bill would supersede all existing consumer remedies, including tort remedies and the right to a jury trial.
>
> For various reasons, ranging from lack of jurisdiction to ineffective means of enforcement, public agencies have been unable to provide construction defect victims with any meaningful remedy. Moreover, under legislation enacted in 1996,

homeowners seeking remedies for construction defects already are subjected to unique and elaborate procedural hurdles which no other civil litigants must endure. This bill would further exacerbate this plight.

A home is a family's largest investment; homeowners are entitled to quality construction. We strongly oppose efforts to deny them the ability to recover damages when they are victims of land subsidence, sinking foundations, water intrusion, structural and fireproofing defects, inadequate seismic bracing, and other construction defects resulting from the negligence of builders and developers.

The Executive Council of Homeowners (ECHO) is strongly opposed to both the bill and its underlying rationale. "ECHO disagrees with the virtually unsupported assertion of the bill's sponsors that construction defect litigation represents the primary cause for reducing the production of multi-family housing or the construction of housing within common interest developments (CIDs). ECHO remains adamantly opposed to the building industry's attempt to eliminate traditional home buyer remedies in exchange for an unproven and inadequately conceived warranty program." The key problems with AB 1221 identified by ECHO are as follows: "The Bill proposes a 'warranty' with no underwriting standards. The Legislation contains an insurance program qualified by a state licensing agency (Contractor's State Licensing Board). There is no demonstrated insurance product to support a mandatory statutory program. AB 1221 does not guarantee that defect recovery will be available from any source, at time of claim. Despite uncertain future funding of defect repairs, AB 1221 asks home buyers to give away all other legal protections and causes of actions against responsible parties."

Prior Related Legislation. AB 1950 (Torlakson), Chapter 856, Statutes of 1998. In its original form, this bill sought to revise the procedures and timeline for the pre-litigation process in construction defect suits designed to encourage settlement of such suits between a builder of a common interest development and a homeowners' association prior to the filing of a lawsuit. This bill was the end product of then-Senator Lockyer's Blue Ribbon Task Force on California's home construction industry. As enacted, the bill was limited to a provision allowing an insurer to provide a defense for a suspended corporation in a civil action based upon a claim for personal injury, property damage, or economic losses against the suspended corporation, and a provision which permits the court to bind parties to settlement agreements which are stipulated to by the parties' counsel rather than the parties themselves.

AB 594 (Torlakson), vetoed. Nearly identical to the original form of AB 1950 (Torlakson), this bill sought to revise the procedures and timeline for the pre-litigation process in construction defect suits designed to encourage settlement of such suits between a builder of a common interest development and a homeowners' association prior to the filing of a lawsuit. This bill was the end product of then-Senator Lockyer's Blue Ribbon Task Force on California's home construction industry.

SB 1029 (Calderon) Chapter 864, Statutes 1995. This measure created the pre-litigation process for construction defect actions relating to common interest developments that has become known in the industry as the "Calderon process."

REGISTERED SUPPORT / OPPOSITION:

Support

Coalition for Quality Affordable Housing (Sponsor)
AMCAL Communities, Inc.
American Institute of Architects, California Council
Avanti Roofing, Inc.
Bay Area Council
Building Industry Association of the San Joaquin Valley
Building Industry Association of Tulare and Kings Counties
California Association of Sheet Metal and Air Conditioning Contractors
California Building Industry Association
California Tile Company
Centrex Homes
Civil Justice Association of California
CNA Insurance Company
Commercial & Industrial Roofing Co. Inc.
Communities Southwest Development and Construction Company
Del Webb California Corporation
Dempsey Insurance Service, Inc.
EAH
Genstar Land Company Southwest
Gibson and Company Insurance Brokers, Inc.
Golden State Fence Co.
Hix Development Corp.
Home Ownership Advancement Foundation
Hunsaker & Associates
Insurance Agents and Brokers Legislative Council
Luce, Forward, Hamilton & Scripps
Martin Roofing Co., Inc.
National Roofing Contractors Association
Northbay Ecumenical Homes
Pacific Bay Homes
Professional Insurance Agents of California and Nevada
Reynolds Communities
Roofing Contractors Association of California
Stout Roofing Inc.
The Corky McMillin Companies
Western Pacific Housing
Western Pacific Roofing Corporation
7 Individuals

Opposition

California Dispute Resolution Council (opposed in part)
Community Associations Institute

Consumer Attorneys of California
Executive Council of Homeowners (ECHO)

Analysis Prepared by: Donna S. Hershkowitz / JUD. / (916) 319-2334